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Current Report

Division of Agricultural Sciences and Natural Resources • Oklahoma State University

Estimating 1999 Federal and State Income Taxes

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Timely Tax Planning Now Can Increase After-Tax Income

This year Congress has provided two new and improved tax management tools to help level year to year income. The 1998 Tax and Trade Relief Act made permanent a 1997 temporary provision to allow agricultural producers to average income over the last three taxable years. Farm income includes Schedule F, sales of capital assets such as breeding livestock, machinery, and equipment, but not land. Any or all of the current year's income can be elected for averaging. The elected farm income is divided into three equal parts and added to the three previous tax years. The marginal increase in tax for the previous years caused by the portion of elected farm income carried back from the current year is combined with tax from the current year. The greatest tax savings result from a very high current year taxable income carried back to years that have very low taxable income. Corporations, estates, and trusts are not allowed to use income averaging. However, an individual, a partner in a partnership, and an S Corporation shareholder can average partnership or S Corporation distributions on their individual tax returns.

The 1998 tax act also extended the number of years that a net operating loss (NOL) could be carried back. Under prior law a (NOL) could be carried back two years to get a refund of taxes paid in those prior years, or carried forward for up to 20 years. Special rules allow a loss that resulted from being in a Federal Disaster Area to be carried back three years. Beginning in 1998, agricultural producers can carry back losses for (5) five years. If the current year's taxable income is negative or a loss, the loss this year may be applied to the five prior years. If taxes were paid in the last five years, the loss could be carried back to generate a refund of those taxes paid.

The USDA has declared many Oklahoma counties as eligible for some form of federal assistance. This declaration allows producers in these counties to use the drought sale of livestock rules for 1999.

Floods and other natural disasters have destroyed or damaged some agricultural crops and livestock. A casualty loss is the damage or total loss of personal or business property from an event that is identifiable, sudden, unexpected, or unusual. Fire, flood, hail, storm, lightning, tornadoes, and auto accidents that are not the result of your negligence are examples of casualty losses.

The tax benefit or deductible loss is limited to either the decrease in Fair Market Value (FMV) or your tax basis, whichever is less. This lesser amount must be further reduced by any insurance proceeds or other salvage value received. Crop insurance proceeds and qualified disaster payments can also be postponed until next year. See Current Report, CR-789, Disaster and Casualty Losses for more detailed information.

Drought sales of breeding livestock sold in excess of normal sales can qualify as involuntary conversion and the tax on gain postponed, if like animals are bought within two years. The taxable gain on the sales of all livestock sold in excess of normal sales can be postponed to next year. See Current Report CR-788, Tax Consequences of Drought Sales of Livestock for more information.

Many legal tax planning alternatives are available to help reduce the tax liability. This Current Report is designed to help you estimate Federal, State, Self-employment, and Alternative Minimum Taxes. An income tax checklist is provided to call attention to infrequent tax events that may greatly affect your tax liability. Use this worksheet as a guide. For specific questions, contact your local OSU County Extension Director, Area Farm Management Specialist, or State Tax Specialist.

Income Tax Check List for Farmers and Ranchers

1. Will taxable income be above or below average? (Check before year end.)
2. Have you sold land or other assets or had debt forgiven? You may owe tax on the sale and the amount of debt forgiven.
3. Have you purchased a farm this taxable year? If yes, consider the importance of allocating costs to land, growing crops, depreciable improvements, dwelling, etc.

4. Can drought sales of breeding livestock be treated as an involuntary conversion this year? Explore the consequences of replacing with similar type property.
5. Have you sold easement or right-of-way this year?
6. Are you planning to sell land in the near future? If yes, consider the use of the installment method to reduce taxes and/or perhaps a trade (spreading income among years).
7. Leases of machinery and equipment not associated with land may be subject to self-employment tax.
8. Are you taking full advantage of the tax credits (Earned income credit, credit for the elderly, and child care credit)?
9. Are payments of estimated tax required to avoid the underpayment penalty?
10. Should you consider an IRA or Koegh plan?
11. Should you consider the alternative method of paying Social Security tax?
12 Could a net operating loss be carried back two or five years to get a tax refund for those years?
13. Will the expensing election (Sect. 179) reduce your taxable income? The maximum amount is $19,000. W-2 wages can be used to offset a farm loss to qualify for the expense election.

1999 Income Tax Estimate Work Sheet

			(1) Amounts to Date	(2) Estimated Rest of Year	(3) Estimated Years Total
(01)	Total Current Farm Sales	(01)			
(02)	Sale of Items Pur. for Resale	(02)			
(03)	Less Pur. Cost of Resale Items	(03)			
(04)	Taxable Inc. from Resale Items (2-3)	(04)			
(05)	Taxable Gain from Capital Assets[A]	(05)			
(06)	Taxable Non-farm Income[B]	(06)			
(07)	Total Taxable Inc. Lines (1+4+5+6)	(07)			
(08)	Total Current Farm Expenses[C]	(08)			
(09)	Annual Depreciation Expense[D]	(09)			
(10)	Self Employment Income[E]	(10)			
(11)	Capital Losses[F]	(11)			
(12)	Total Deductions Lines (8+9+11)	(12)			
(13)	Adjusted Gross Income Line (7-12)	(13)			
(14)	Personal Exemptions $2,750 x No.____	(14)			
(15)	Standard or Itemized Deductions[G]	(15)			
(16)	Taxable Income Lines (13-14-15)	(16)			
(17)	Estimated Income Tax[H]	(17)			
(18)	Total Tax Credits	(18)			
(19)	Estimated Tax Due (17-18)	(19)			
(20)	OK Income Tax Due[I]	(20)			
(21)	Self-Employment Tax[J]	(21)			
(22)	Alternative Minimum Tax[K]	(22)			
(23)	Employment Taxes[L]	(23)			

Footnotes

A. 100% of gain above losses. (100% of gain resulting from depreciation taken on purchased breeding cattle, machinery, and equipment sold.)

B. Off-farm employment, rent, oil income, etc. A depletion deduction may be allowed against oil income.

C. Exclude capital purchases and cost of cattle purchased for resale.

D. Last year, plus depreciation on new items.

E. Self-Employment Income = (line 1 + line 4) - (line 8 + line 9).

F. 100% of capital losses up to $3,000 in excess of short term gains and capital gains may be deducted for years after 1989. ($3,000 net losses can be a current deduction that offsets other income)

G. If your itemized deductions are greater than standard deduction ($4,300 single, $7,200 married, filing jointly), the larger amount should be deducted from your adjusted gross income before using the tax rate schedule.

H. Multiply line 16 by the appropriate value in the Federal Tax Rate Schedule Table 1.

I. First calculate Oklahoma Taxable Income: (OTI) Line 13 - (number of personal exemptions x 1,000) - ([the larger of federal itemized deductions] or [15% of Line 13 not to exceed $2,000]).

Then multiply OTI by the appropriate line in Table 2, Method 1,

or

Subtract Federal Tax Line 19 from (OTI) and multiply by the appropriate line in Table 2, Method 2. Oklahoma tax due is the smaller tax calculated under Methods 1 and 2.

J. Self-employment tax = (line 10 x (1-.0765)) x 15.30%.

K. Alternative minimum tax = [(adjusted gross income, Line 13, + Tax Preference Item 1) - Alternative minimum tax adjustments 2 - alternative minimum tax exemption 3] * Tax rate 4

1. Tax preference items include accelerated depreciation of real property, accelerated depreciation of leased personal property, amortization of certified pollution control facilities, appreciated property charitable deduction, incentive stock options, tax exempt interest from private activity bonds, intangible drilling costs, depletion, and reserves for losses on bad debts of financial institutions.
2. Alternative minimum adjustments include standard deduction, medical and dental expense, miscellaneous itemized deductions, taxes, interest, other interest adjustments, depreciation of property, circulation and research and experimental expenditures, mining exploration and development costs, long-term contracts, pollution control facilities, installment sales, basis adjustment, certain loss limitations, tax shelter farm loss, passive activity loss, and beneficiaries of estates and trusts.
3. Alternative minimum tax exemption -
   Single filers = $33,750
   Joint return and surviving spouses =$45,000
   Married filing separately = $22,500
4. Tax rate = 26% on AMT income up to $175,000
   28% on AMT income above $175,000

L. Congress passed legislation which requires farmers to withhold federal and state income tax from cash wages and salaries paid to agricultural employees. Under prior law, agricultural workers were not subject to income tax withholding after December 31, 1989. Wages paid to farm workers will generally be subject to income tax withholding if the cash wages earned by the agricultural workers are subject to FICA (Social Security) withholding. FICA withholding applies generally if the worker earns more than $150 or the employer pays $2500 to all agricultural workers. Wages paid to family members under 18 years of age are exempt from FICA withholding. Thus, these family youth are also exempt from income tax withholding. Wages paid to a spouse employed on the family farm and children 18 and over are subject to FICA and are therefore subject to withholding.

Table 1. 1999 Income Tax Rate Schedules.

Married Individuals Filing Joint Returns and Surviving Spouses

If taxable income is:	The tax is:
Not over $43,050	15% of taxable income
Over $43,050 but not over $104,050	$6,457.50 plus 28% of the excess over $43,050
Over $104,050 but not over $158,550	$23,537.50 plus 31% of the excess over $104,050
Over $158,550 but not over $283,150	$40,432.50 plus 36% of the excess over $158,550
Over $283,150	$85,288.50 plus 39.6% of the excess over $283,150

Heads of Household

If taxable income is:	The tax is:
Not over $34,550	15% of taxable income
Over $34,550 but not over $89,150	$5,182.50 plus 28% of the excess over $34,550
Over $89,150 but not over $144,400	$20,470.50 plus 31% of the excess over $89,150
Over $144,400 but not over $283,150	$37,598.00 plus 36% of the excess over $144,400
Over $283,150	$87,548.00 plus 39.6% of the excess over $283,150

Table 1. (continued)

Unmarried Individuals (Other Than Surviving Spouses and Heads of Household)

If taxable income is:	The tax is:
Not over $25,750	15% of taxable income
Over $25,750 but not over $62,450	$3,862.50, plus 28% of the excess over $25,750
Over $62,450 but not over $130,250	$14,138.50, plus 31% of the excess over $62,450
Over $130,250 but not over $283,150	$35,156.50, plus 36% of the excess over $130,250
Over $283,150	$90,200.50, plus 39.6% of the excess over $283,150

Married Individuals Filing Separate Returns

If taxable income is:	The tax is:
Not over $21,525	15% of taxable income
Over $21,525 but not over $52,025	$3,228.75, plus 28% of the excess over $21,525
Over $52,025 but not over $79,275	$11,768.75, plus 31% of the excess over $52,025
Over $79,275 but not over $141,575	$20,216.25, plus 36% of the excess over $79,275
Over $141,575	$42,644.25, plus 39.6% of the excess over $141,575

Table 2. 1999 Oklahoma Tax Rate Schedule.

METHOD I

Married Filing Jointly or Head of Household

IF TAXABLE INCOME IS:

$-0-	-	$2,000	Pay 1/2 of 1% of taxable income	
2,000	-	5,000	Pay $10.00 + 1% over	$2,000
5,000	-	7,500	Pay 40.00 + 2% over	5,000
7,500	-	9,800	Pay 90.00 + 3% over	7,500
9,800	-	12,200	Pay 159.00 + 4% over	9,800
12,200	-	15,000	Pay 255.00 + 5% over	12,200
15,000	-	21,000	Pay 395.00 + 6% over	15,000
21,000		over	Pay 755.00 + 7% over	21,000

METHOD II

Married Filing Jointly or Head of Household

IF TAXABLE INCOME IS:

$-0-	-	$2,000	Pay 1/2 of 1% of taxable income	
2,000	-	5,000	Pay $10.00 + 1% over	$2,000
5,000	-	7,500	Pay 40.00 + 2% over	5,000
7,500	-	8,900	Pay 90.00 + 3% over	7,500
8,900	-	10,400	Pay 132.00 + 4% over	8,900
10,400	-	12,000	Pay 192.00 + 5% over	10,400
12,000	-	13,250	Pay 272.00 + 6% over	12,000
13,250	-	15,000	Pay 347.00 + 7% over	13,250
15,000	-	18,000	Pay 469.50 + 8% over	15,000
18,000	-	24,000	Pay 709.50 + 9% over	18,000
24,000	-	over	Pay 1,249.50+10%over	24,000

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